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COLCEL

COLCEL COLUMBIA CELLULOSE COMPANY, LIMITED ANNUAL REPORT 1968

VANCOUVER, BRITISH COLUMBIA

CONTENTS

During 1968 Columbia Cellulose introduced its distinctive new housemark shown on the front cover of this report. The trademark officially adopts the abbreviation "COLCEL" and associates it with trees in the design of a "C", symbolizing the forest resources which form the backbone of the company's major fields of endeavour.

TRANSFER AGENTS

COMMON	Montreal Trust Company – *Vancouver, Toronto, Montreal*
	Bankers Trust Company – *New York*
PREFERRED	The Royal Trust Company – *Vancouver, Toronto, Montreal, Winnipeg and Halifax*

REGISTRARS

COMMON	The Royal Trust Company – *Vancouver, Toronto, Montreal*
	The Chase Manhattan Bank – *New York*
PREFERRED	The Royal Trust Company – *Vancouver, Toronto, Montreal, Winnipeg and Halifax*

STOCK LISTINGS

VANCOUVER, TORONTO AND MONTREAL STOCK EXCHANGES

AUDITORS

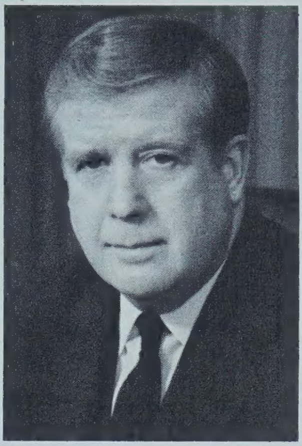
PEAT, MARWICK, MITCHELL & CO., *Vancouver*

REGISTERED OFFICE

1200 - 1111 WEST HASTINGS STREET, VANCOUVER 1, B.C.

COLCEL
COLUMBIA CELLULOSE COMPANY, LIMITED
1111 WEST HASTINGS STREET, VANCOUVER 1, B.C., CANADA. TELEPHONE: 685-2452

TO THE SHAREHOLDERS



Net loss for the year amounted to $9,478,339, as compared with $10,776,341 in the previous year after giving effect to the change in accounting policy stated in the notes to the consolidated financial statement. Record net sales of $88,155,783 represent a substantial increase over sales of $67,494,994 in 1967. Gross billings in 1968 exceeded $100,000,000, also a record for the company.

It is encouraging to note that net loss on operations, before taxes and minority interests, was $9,751,339, an improvement over the loss of $16,627,486 in 1967. The funds generated by operations were $1,910,826, as opposed to a deficit of $6,838,170 in the previous year. This improvement in funds from operations enabled the company to arrest the cash drain of the previous year, and to finance with no outside borrowings other than normal bank loans.

The results of operations for 1968, and the comparative figures for 1967, reflect the adoption of a more conservative accounting policy. Mill start-up expenses are to be charged to operations as incurred, rather than deferred and amortized over the first five years of good production.

Despite generally adverse market conditions, the company successfully marketed its greatly increased tonnages of bleached kraft and sulphite dissolving pulp grades during 1968. The better supply and demand relationship expected in 1969 will allow the company to concentrate its selling efforts in the geographical areas and product lines offering the highest profit potential.

The Prince Rupert sulphite and kraft mills share auxiliary facilities and are jointly operated. Difficulties attendant in the start-up of the Skeena mill plagued both operations in early 1968. Management concentrated maintenance activity on the Skeena Kraft mill initially, and a more level production rate and better product quality were achieved as the start-up difficulties were overcome. Subsequently, the sulphite mill was given special maintenance attention, and restored to good working order. Now that the production processes of these two mills have been stabilized, the emphasis will be on profit improvement through cost reduction and productivity increases, both of which have good potential.

A strike in the Interior started in 1967 and shut down all company operations in the area until January, 1968. In mid-year, labour contracts were negotiated with hourly workers at the pulp mills and Northern woods operations. No lost time was sustained during these negotiations. No labour contracts expire during 1969.

Pulp production at Castlegar approached an all-time high, and the performance of the sawmill exceeded that of any previous year. Despite increased labour and stumpage rates, wood costs were in line with past experience.

During 1968 log costs to the Prince Rupert mills were reduced materially. A new management team was established at Twinriver Timber Limited and plans made for further substantial cost reductions in 1969.

In July 1968, Svenska Cellulosa Aktiebolaget (S.C.A.) exchanged its minority interest in Skeena Kraft Limited for common shares in the company. Simultaneously, S.C.A. purchased 1,230,000 additional common shares in the company held by Celanese Corporation. Skeena Kraft Limited is now a wholly-owned subsidiary of Columbia Cellulose Company, Limited, as Celgar Limited has been since inception. Economies of operation are possible now that these two subsidiary companies can be managed as an entity.

Our objectives for 1968 have been achieved. We have stopped the drain on cash resources; we have introduced reliability and stability into the production processes at the Prince Rupert pulp mill complex; we have built a strong management team and consolidated many of the management and service functions; and we have come through a period of serious market imbalance. The company is in a position to show further market improvement in 1969.

We attribute the success in meeting our goals for 1968 to the dedication of the management team, and to the co-operation of the company's employees.

Future emphasis will be on profit improvement through cost reduction and productivity increases. The benefit from these activities is becoming evident in the first quarter of 1969 and the full impact will be apparent later in the year.

On behalf of the Board,

GEORGE W. SCRIMSHAW,
President and Chief Executive Officer.

April 18, 1969 – Vancouver, B.C.

COLCEL **COLUMBIA CELLULOSE COMPANY, LIMITED** *and its subsidiary companies*

FINANCIAL SUMMARY AND REVIEW *(in thousands of dollars)*

	1959	1960	1961	1962	1963	1964	1965	1966	1967	1968
Net sales	$ 26,131	$ 26,223	$ 37,823	$ 51,907	$ 56,768	$ 62,347	$ 65,530	$ 64,397	$ 67,495	**$ 88,156**
Profit on operations before the undernoted	6,932	6,027	6,995	14,048	17,431	18,652	16,725	10,699	(1,132)	**8,888**
Cost of borrowed money (net)	886	899	2,387	3,356	3,886	3,992	3,691	4,313	7,285	**7,231**
Depreciation, amortization and depletion	3,141	3,056	3,940	5,625	5,814	6,241	6,290	6,944	8,210	**11,408**
Net profit (loss) before income taxes	2,905	2,072	668	5,067	7,731	8,419	6,744	(558)	(16,627)	**(9,751)**
Provision for income taxes (recovery)	—	—	1,249	1,138	3,527	4,160	3,220	1,527	(3,205)	**(273)**
Minority shareholder's interest in loss of subsidiary	—	—	—	—	—	—	—	(1,354)	(2,646)	—
Net profit (loss) for the year	2,905	2,072	(581)	3,929	4,204	4,259	3,524	(731)	(10,776)	**(9,478)**
Current assets:									54 m.	
Cash and equivalent	5,262	4,077	3,662	9,084	6,899	4,275	16,013	11,924	9,039	**6,843**
Inventories	4,731	10,946	12,487	11,251	14,216	14,949	17,923	22,831	31,469	**29,132**
Other current	2,504	2,055	4,161	6,047	6,667	7,724	9,978	10,510	14,908	**16,661**
	12,497	17,078	20,310	26,382	27,782	26,948	43,914	45,265	55,416	**52,636**
Current liabilities	4,686	5,310	6,022	7,029	9,095	7,538	9,680	24,718	25,863	**28,233**
Working capital	7,811	11,768	14,288	19,353	18,687	19,410	34,234	20,547	29,553	**24,403**
Property, plant and equipment, at cost	77,449	107,584	118,347	123,185	130,450	138,510	170,478	220,590	225,436	**227,386**
Accumulated depreciation, amortization and depletion	20,232	22,582	26,509	31,286	36,381	40,893	46,809	52,373	57,634	**67,447**
Net fixed assets	57,217	85,002	91,838	91,899	94,069	97,617	123,669	168,217	167,802	**159,939**
Long-term debt	29,228	34,138	43,501	61,973	61,842	61,792	105,358	114,325	125,552	**105,379**
Minority interest	—	—	—	—	—	—	4,000	2,646	—	—
Preferred shares (par value)	—	10,000	25,000	7,500	5,000	5,000	20,750	20,750	20,750	**20,750**
Common equity	37,621	39,329	38,049	41,278	43,608	46,042	47,311	45,584	33,812	**38,496**

Adjusted for Celgar and Skeena pre-operating expenses charged off as incurred.

FINANCIAL HIGHLIGHTS

Net sales for 1968 were $88,155,783, an increase of $20,660,789 over 1967 due largely to higher production rates and settlement of a strike which had carried over from 1967. Gross sales for 1968 were $100,251,435.

Results for the year were severely hampered by the high, although improving, costs in the Skeena Kraft operation. Other units showed substantial improvement. Skeena Kraft, which commenced production in 1966, had a loss before depreciation of $6,252,897 in the current year which is an improvement of $3,511,132 over the 1967 loss of $9,764,029. Skeena's net loss was $9,000,466 down by $1,197,664 from $10,198,130 in 1967. Celgar Limited reduced its pre-tax loss to $614,109 from $6,477,991 in 1967, an improvement of $5,863,882.

The consolidated net loss before income taxes and minority interest was reduced to $9,751,339 in 1968 from $16,627,486 in 1967, an improvement of $6,876,147. Consolidated net loss after all items was $9,478,339 as compared to $10,776,341 in 1967. Due to an improvement in Celgar operations the credit from deferred income taxes was lower by $2,932,000 in 1968. Skeena Kraft Limited has not recognized in its accounts future income tax benefits of approximately $11,200,000 which are available for claim against taxes of future years. Accumulated losses in Skeena exceeded its share capital at the end of 1967 with the result that no portion of the 1968 loss was allocated to minority interest.

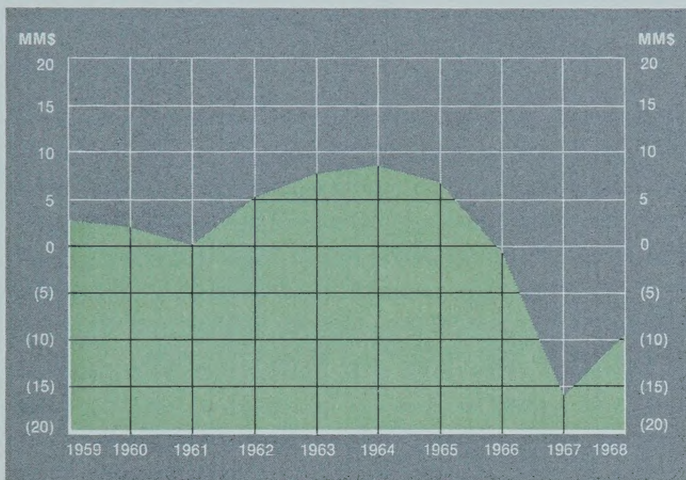
Cash was generated from operations in the amount of $1,910,826 as compared with a cash deficit of $6,838,170 in 1967, an improvement of $8,748,996. This was due to the improvement in earnings before credits for deferred income taxes and minority interest and an increase in depreciation and other non-cash charges sustained in 1968.

Capital expenditures during the year amounted to $3,983,335 as compared to $11,090,830 in 1967, a decrease of $7,107,495. At December 31, 1968, the investment in property, plant and equipment totalled $227,386,455 and the accumulated depreciation, depletion and amortization totalled $67,447,370.

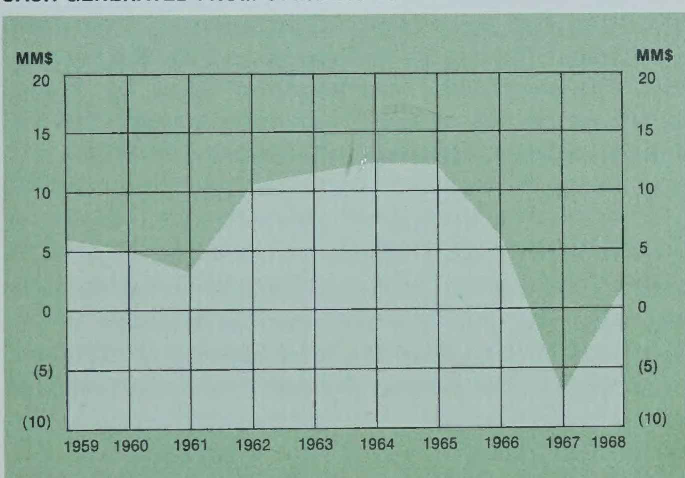
On January 2, 1969 the regular payment on principal of U.S. $4,000,000 was made to the holders of Celgar 6⅛% First Mortgage Bonds. Long-term debt was reduced by $15,900,000 resulting from the purchase as at July 1, 1968 of the minority interest (stock and debentures) in Skeena Kraft for 3,125,000 common shares of Columbia Cellulose. During the year working capital decreased by $5,149,740 to $24,402,903.

The financial results, comments and ten year Financial Summary and Review have been stated in accordance with the change in accounting policy for this group of companies. For details refer to Note 11 of the notes to the Consolidated Financial Statements.

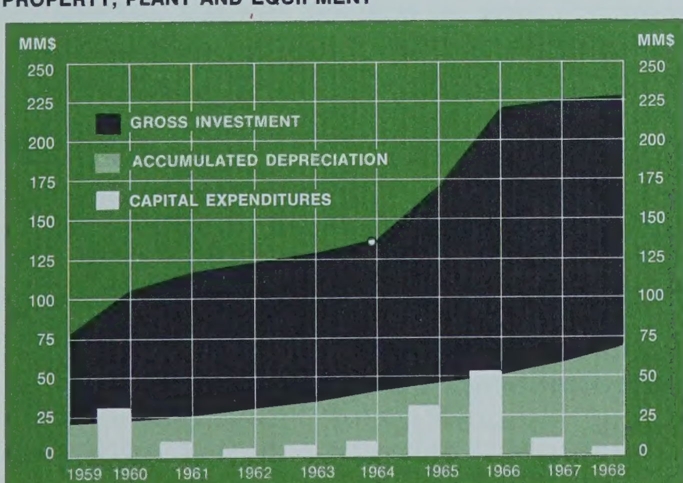
PROFITS (LOSSES) BEFORE TAXES AND MINORITY INTEREST



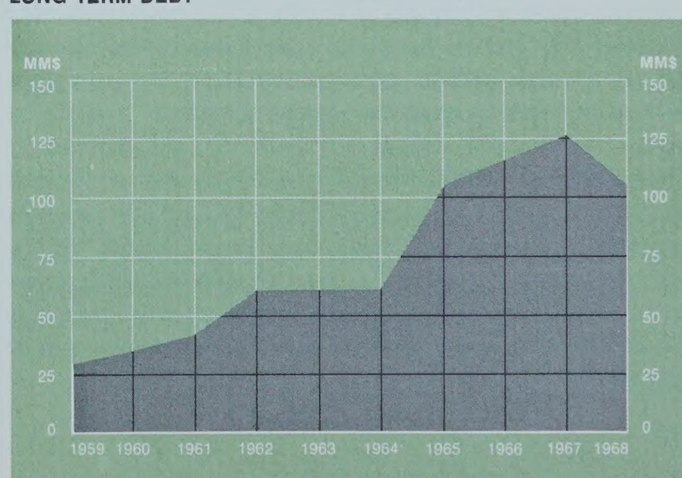
CASH GENERATED FROM OPERATIONS



PROPERTY, PLANT AND EQUIPMENT



LONG TERM DEBT



COLUMBIA CELLULOSE COMPANY, LIMITED *and its subsidiary companies*

OPERATIONS

Columbia Cellulose is a diversified forest products company manufacturing a wide range of sulphite and kraft pulps and lumber. Incorporated in 1948, the company now consists of five operating divisions including three large, modern pulp mills, a modern, double sawmill and two extensive forestry divisions. Employing approximately 2,800 persons, it is the major enterprise in most of the communities close to its operations. Timber reserves are held in three Tree Farm Licences containing a total of more than 3,000,000 productive acres of forest land. These are situated in interior climatic regions giving very desirable tree species and growth characteristics for high quality pulp manufacture. All the company's timber lands are under a programme of perpetual forest management.

TREE FARM LICENCE NO. 1

The company pioneered in the Tree Farm Licence system in 1948 when T.F.L. No. 1 was awarded to the company to provide the necessary raw material to substantiate the construction of a pulp mill. The area contains 840,000 acres of productive forest land in the Nass and Skeena River watersheds. The C.N.R. system through the Skeena Valley provides an important transportation link to supplement the two vital water transportation routes to Prince Rupert.

PRINCE RUPERT SULPHITE MILL

The original sulphite mill in 1951 was designed to produce 200 tons per day of dissolving pulp to replace cotton linters in the manufacture of acetate textiles. The plant has since been expanded to a capacity of more than 560 tons per day and its product range extended to include grades for the manufacture of acetate, tri-acetate and viscose textiles, and chemicals and plastics.

TREE FARM LICENCE NO. 23

In 1951 Columbia Cellulose bought timber and sawmill interests in the central Arrow Lakes area of British Columbia and later obtained T.F.L. No. 23 with 890,000 acres of productive forest land. A key feature of the licence is the short haul to water and the downstream movement of logs to the mills at Castlegar.

CASTLEGAR MILLS

In 1959 and 1960 the closely integrated pulp mill and sawmill complex went into production at Castlegar. The mills are designed to ensure maximum use of forest resources by a mutual exchange of logs, chips, hog fuel, steam, heat and high pressure water. The pulp mill is now rated at more than 600 tons per day of bleached kraft and the sawmill at 120 million board feet per year.

TREE FARM LICENCE NO. 40

In 1964 T.F.L. No. 40 was issued supporting a new pulp mill project in conjunction with the existing Prince Rupert Operations. This comprises 1,400,000 acres of productive forest land in the interior reaches of the Nass River watershed. The contiguous relationship of T.F.L. No. 1 and No. 40 permits the company to enjoy the benefits of combined management of these two forestry units.

PRINCE RUPERT KRAFT MILL

In early 1967, the world's largest and most modern single-line kraft pulp mill was put into operation at Prince Rupert. Since that time the many operating problems connected with the start-up of a new mill of this size have been met and overcome. The mill demonstrates a potential for high quality bleached kraft production in excess of 850 tons per day.

DEVELOPMENT CENTRE

The company has maintained advanced facilities for wood cellulose research since 1952. Originally directed towards dissolving pulp and textile studies, emphasis has been changed to include paper pulps. Today, the Dissolving Pulp Development Department and the Paper Pulp Development Department are directly involved in providing technical assistance to the operations through short-range studies geared to cost control and product improvement. From its location near Vancouver, the development centre also provides technical assistance to customers.

COLUMBIA CELLULOSE COMPANY, LIMITED *and its subsidiary companies*

MARKETS

Dissolving pulps are in strong demand with an estimated growth of 5% to 6% per annum forecast for viscose and acetate fibres in the European and Japanese markets. The tri-acetate pulp developed by the company for the manufacture of Arnel* is one of the most versatile of the manmade fashion fibres today.

Our kraft pulps are finding ready acceptance in world markets. A strengthening U.S. demand is enabling our Castlegar mill to increase its sales of Celgar Kraft into that area. Skeena Kraft has been received favourably in world export markets due to its superior quality. Several specialty grades of kraft paper pulp have been produced for specific customers and other grades have been successfully introduced to the market. These specialties can be counted on to diversify and stabilize sales during 1969.

Current indicators for home building and construction in North America give good reason for anticipating continued growth in lumber markets. Throughout 1968 these markets expanded, providing steady sales for all segments of the B.C. industry including the Celgar Sawmill. Major markets for Celgar brand lumber were in the central and northeastern United States. A significant part of our lumber production also moved to Eastern Canada.

The bulk of production in all grades of lumber and pulp was sold in markets outside of Canada. Europe and the Far East have taken increasing amounts of pulp and offer the brightest long-term prospects for sales. Coincidentally, these areas are supplying Canada with large amounts of consumer goods and heavy equipment. The cost of such imports is balanced to a considerable degree by foreign credits earned through exports of forest products.

World demand has definitely improved, and it is anticipated that these better business conditions will continue to be reflected in strengthening prices. The strength shown in the current market is expected to be sufficient to ensure full operation of our mills through 1969.

OUTLOOK

Improving production performance, rigid controlling on expenditures, building a strong management team, curtailing outside borrowings – these have been the keys to strengthening the company's position to the end of 1968.

It is evident that further advantages can be gained from modification of processes and procedures in the combined facilities at the Prince Rupert pulp complex. Pulp and lumber operations in the Castlegar area are situated in close proximity to the main pulp and lumber markets in the U.S. and Canada. They can be expected to contribute substantially to the 1969 earnings picture in view of ready market acceptance and continuing programmes of cost control and process improvement.

We enter the year with low inventories, a situation which faces the entire B.C. industry due to the extremely severe weather conditions in British Columbia this year. There is little likelihood of inventory rebuilding until the second quarter. This situation, together with the ready acceptance of the quality of our new pulps in overseas markets, will enable us to concentrate on market areas and products which offer the greatest profit potential.

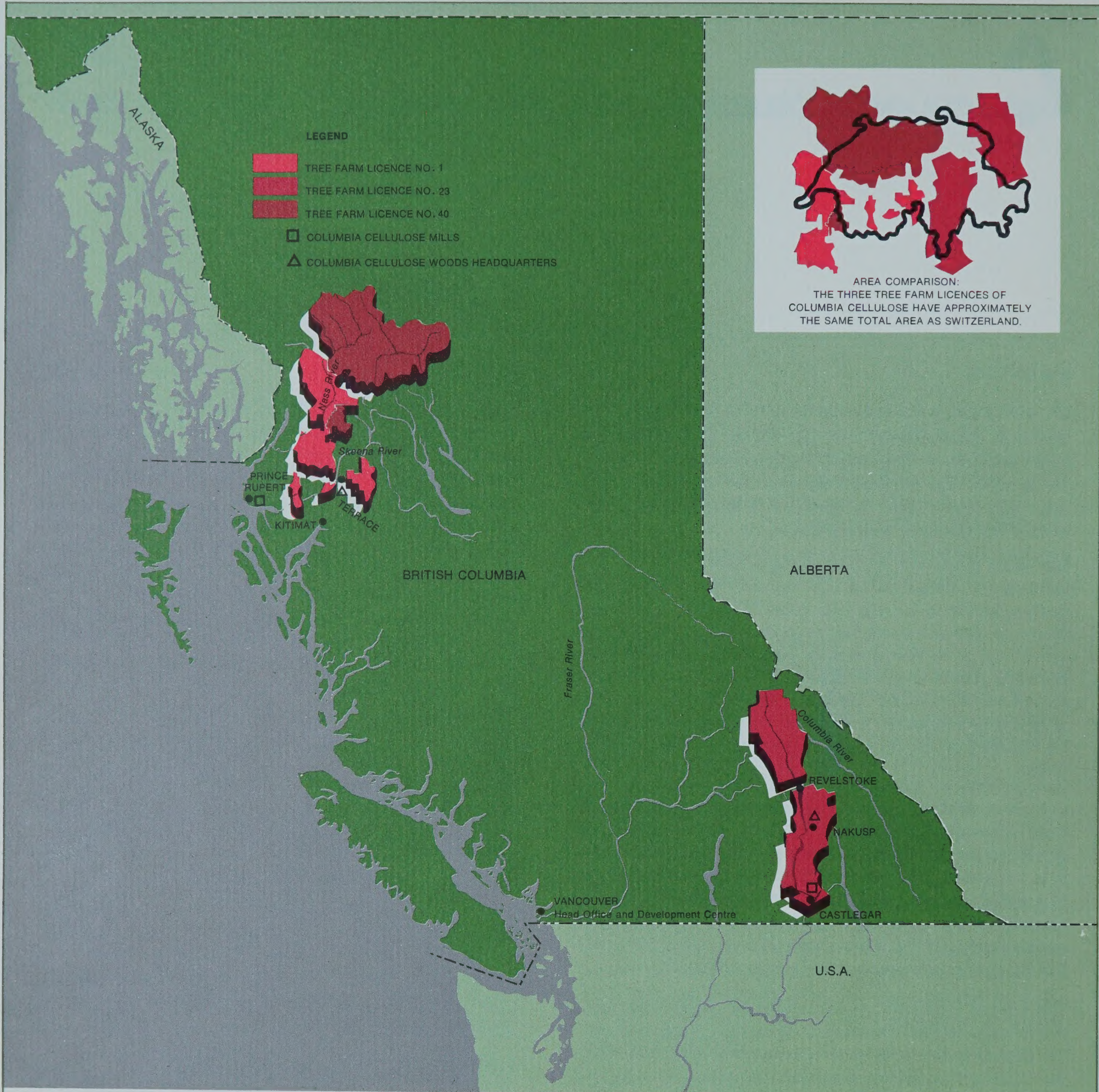
Columbia Cellulose has excellent resources and facilities. The accomplishments of 1968 form a firm basis for further opportunity and improvement. The present management group is determined to create and maintain a strong, self-reliant company, able to take an important place within the business community.

EMPLOYEES AND COMMUNITIES

Our successful efforts to reduce costs and increase efficiencies are attributable to the co-operation of all our employees. Columbia Cellulose personnel form an important segment of their communities, and their contributions to civic government and social life are noteworthy.

Columbia Cellulose operations have a major impact on nearby communities, providing steady employment and regular payrolls, and supporting local merchants by the purchase of supplies and services.

*Registered Trademark.



COMPANY OPERATIONS

The head office of Columbia Cellulose is in Vancouver with the development centre located on Annacis Island in the Vancouver area.

The company manages a total area of some 9,000,000 acres of which 3,000,000 acres are classified as productive forest land. This total acreage is approximately equal to the whole land area of Switzerland.

Tree Farm Licences Nos. 1 and 40 combine to give 2.2 million productive acres supplying a major part of the wood requirements of the Prince Rupert sulphite and kraft mills. Administered from Terrace, these timberlands lie in the Nass and Skeena Valleys relying on water, rail and truck transportation to the mills.

Tree Farm Licence No. 23, with 890,000 productive acres, supplies the sawmill and kraft pulp mill complex at Castlegar. The woods division offices are at Nakusp.

Columbia Cellulose manufactures a wide range of pulps which can be converted into acetate, tri-acetate and rayon textiles; plastics; chemicals; fine and utility papers; and an infinite variety of paper and paperboard products at the high quality end of the processing scale.

Celgar Lumber is a reliable building materials supplier with a wide selection of grades, sizes, and species for the construction and home building industries.

WORLD MARKETS

The above map indicates a dramatic change in the market distribution of Columbia Cellulose pulps compared to five years ago. The U.S. market, which in 1963 took 67% of our sales volume, now takes 45% although its gross tonnage purchases have not changed appreciably. The significant shifts have been towards Europe, which now takes 31% compared to 13% in 1963 and to the Far East which takes 17% compared to 8% in 1963.

Columbia Cellulose is now a major contributor to Canada's foreign exchange earnings, converting the forest resources of British Columbia into purchasing power for imports.

The sales organization and traffic and shipping systems have been reconstructed to meet the changing marketing emphasis with greater efficiency and economy. The dots on the map indicate places where the company is represented.

Accompanying the map presentation are graphs showing past and projected changes in world pulp demand related to consumption of paper and paperboard products and world population trends. These data demonstrate the growing world need for the products we produce and the importance of sustaining a strong international marketing capability.

COLUMBIA CELLULOSE COMPANY, LIMITED *and its subsidiary companies*

CONSOLIDATED STATEMENT OF EARNINGS

for the year ended December 31, 1968 with 1967 comparison

	1968	1967 (Restated)
Net sales	$88,155,783	67,494,994
Cost of goods sold	75,212,584	63,167,590
Selling, administrative and research expenses	4,055,388	5,242,975
Depreciation, amortization and depletion	11,408,023	7,912,543
	90,675,995	76,323,108
Operating loss	(2,520,212)	(8,828,114)
Interest on long-term debt	6,517,984	6,613,739
Other interest, less interest income $101,286	539,288	463,846
Exchange loss on repayment of mortgage bonds	173,855	207,855
Non-recurring loss (net)	—	513,932
Net loss before undernoted items	(9,751,339)	(16,627,486)
Reduction in deferred income taxes (Note 6)	273,000	3,205,000
Net loss before minority interest	(9,478,339)	(13,422,486)
Minority interest in loss of subsidiary	—	2,646,145
Net loss for the year (Note 11)	$ (9,478,339)	(10,776,341)

CONSOLIDATED STATEMENT OF RETAINED EARNINGS (DEFICIT)

for the year ended December 31, 1968 with 1967 comparison

	1968	1967 (Restated)
Balance at beginning of year:		
Previously reported	$ 8,118,014	13,230,038
Adjustment of mill start-up and pre-operating expenses (Note 11)	(8,691,099)	(2,030,782)
Restated	(573,085)	11,199,256
Net loss for the year	(9,478,339)	(10,776,341)
Dividends paid on preferred shares	(498,000)	(996,000)
Accrued dividends on preferred shares of subsidiary company (Note 7)	(497,551)	—
	(10,473,890)	(11,772,341)
Balance at end of year	$(11,046,975)	(573,085)

See accompanying notes to consolidated financial statements.

COLUMBIA CELLULOSE COMPANY, LIMITED *and its subsidiary companies*

CONSOLIDATED STATEMENT OF SOURCE AND APPLICATION OF FUNDS

for the year ended December 31, 1968 with 1967 comparison

	1968	1967 (Restated)
SOURCE OF FUNDS:		
Net loss	$ (9,478,339)	(10,776,341)
Provision for depreciation, amortization and depletion	11,408,023	7,912,543
Minority interest in loss of subsidiary	—	(2,646,145)
Reduction in deferred income taxes	(273,000)	(3,205,000)
Other charges not involving an outlay of funds	254,142	1,876,773
Funds generated by operations	1,910,826	(6,838,170)
Other sources:		
Issue of common shares for minority interest in Skeena Kraft Limited	15,656,250	—
Issue of long-term debt by subsidiary	—	15,133,219
Issue of preferred shares by subsidiary	—	15,000,000
Disposal of fixed assets	294,704	1,853,310
Other	1,399,210	795,633
Total funds provided	19,260,990	25,943,992
APPLICATION OF FUNDS:		
Acquisition of minority interest in Skeena Kraft Limited	15,656,250	—
Capital expenditures	3,983,335	11,090,830
Reduction of long-term debt	4,273,145	4,851,883
Dividends paid	498,000	996,000
Total funds applied	24,410,730	16,938,713
INCREASE (DECREASE) IN WORKING CAPITAL	(5,149,740)	9,005,279
WORKING CAPITAL AT BEGINNING OF YEAR	29,552,643	20,547,364
WORKING CAPITAL AT END OF YEAR	$24,402,903	29,552,643

See accompanying notes to consolidated financial statements.

AUDITORS' REPORT TO THE SHAREHOLDERS

We have examined the consolidated balance sheet of Columbia Cellulose Company, Limited and its subsidiaries as of December 31, 1968 and the consolidated statements of earnings, retained earnings (deficit) and source and application of funds for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the companies at December 31, 1968 and the results of their operations and the source and application of their funds for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year, after giving retroactive effect to the change in the method of accounting for mill start-up expenses as described in Note 11 of the notes to the consolidated financial statements.

Vancouver, British Columbia, February 24, 1969. PEAT, MARWICK, MITCHELL & CO., *Chartered Accountants.*

COLUMBIA CELLULOSE COMPANY, LIMITED *and its subsidiary companies*

CONSOLIDATED BALANCE SHEET

ASSETS

	1968	1967 (Restated)
CURRENT ASSETS:		
Cash and short-term bank deposits	**$ 6,843,013**	9,038,851
Accounts receivable:		
Trade	**11,453,364**	8,896,759
Other	**2,639,686**	3,414,455
Subscriptions receivable (Note 7)	**2,500,000**	2,500,000
Inventories (Note 2)	**29,131,986**	31,468,606
Prepaid expenses	**68,338**	96,861
Total current assets	**52,636,387**	55,415,532
MORTGAGES, DEPOSITS AND PROPERTY HELD FOR DISPOSAL	**725,211**	2,368,028
PROPERTY, PLANT AND EQUIPMENT, AT COST:		
Timber cutting rights, roads and related facilities	**24,485,146**	22,804,669
Buildings, machinery and equipment	**202,359,841**	202,109,240
	226,844,987	224,913,909
Less accumulated depreciation, amortization and depletion (Notes 3 and 8)	**67,447,370**	57,634,383
	159,397,617	167,279,526
Land	**541,468**	522,291
	159,939,085	167,801,817
DEFERRED CHARGES, LESS AMOUNTS WRITTEN OFF:		
Timber reconnaissance	**757,443**	808,838
Debt financing expenses	**621,548**	681,098
Retirement plan contributions (Note 4)	**526,000**	526,000
	1,904,991	2,015,936
TOTAL ASSETS	**$215,205,674**	227,601,313

See accompanying notes to consolidated financial statements.
Subject to the accompanying report of Peat, Marwick, Mitchell & Co., Chartered Accountants, dated February 24, 1969.

December 31, 1968 with 1967 comparison

LIABILITIES AND SHAREHOLDERS' EQUITY

	1968	1967 (Restated)
CURRENT LIABILITIES:		
Bank loans, unsecured	**$ 11,352,250**	9,029,600
Accounts payable and accrued charges	**9,573,339**	8,738,178
Accrued bond interest	**2,860,895**	3,015,990
Long-term debt due within one year	**4,447,000**	5,079,121
Total current liabilities	**28,233,484**	25,862,889
LONG-TERM DEBT (Note 5):		
First mortgage bonds	**92,531,248**	96,647,393
Subordinated debentures of subsidiary	**—**	15,900,000
6% notes payable to a shareholder	**12,148,063**	12,148,063
Timber sales purchase agreement, secured	**700,000**	857,000
	105,379,311	125,552,456
DEFERRED INCOME TAXES (Note 6)	**6,351,000**	6,624,000
PREFERRED SHARES OF SUBSIDIARY (Note 7)	**15,497,551**	15,000,000
SHAREHOLDERS' EQUITY (Notes 8 and 11):		
Share capital:		
$1.20 cumulative redeemable convertible preferred shares of $25 each Authorized and issued 830,000 shares	**20,750,000**	20,750,000
Common shares of no par value Authorized 17,500,000 shares; issued 10,528,803 shares	**50,011,544**	34,355,294
	70,761,544	55,105,294
Contributed surplus	**29,759**	29,759
Deficit	**(11,046,975)**	(573,085)
	59,744,328	54,561,968
COMMITMENTS (Note 9)		
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	**$215,205,674**	227,601,313

Approved on behalf of the Board:

GEORGE W. SCRIMSHAW, *Director.*

CHARLES C. LOCKE, Q.C., *Director,*

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *December 31, 1968*

1. CONVERSION OF FOREIGN CURRENCIES:

Current assets and current liabilities in foreign currencies have been converted into Canadian dollars at the rates of exchange in effect at December 31, 1968. The long-term debt payable in U.S. funds, other than the amount due within one year, has been converted at rates prevailing at the time of receipt of the funds.

2. INVENTORIES:

Finished goods have been valued at the lower of average cost or net realizable value. Other inventories have been valued at the lower of average cost or replacement cost. A summary of the inventories is as follows:

	1968	1967
Raw materials	$18,081,057	21,809,654
Work in process	124,166	87,408
Finished goods	7,606,046	5,806,197
Stores and supplies	3,320,717	3,765,347
	$29,131,986	31,468,606

3. PROPERTY, PLANT AND EQUIPMENT:

Depreciation on pulp mills and the sawmill has been calculated on the straight-line method at 4% on cost and on other assets on the diminishing balance method at varying rates up to 20% a year.

4. DEFERRED RETIREMENT PLAN CONTRIBUTIONS:

No charge has been made to 1968 earnings with respect to retirement plan costs since there was no decrease in the year in the excess of the pension fund assets over liabilities.

5. LONG-TERM DEBT:

First mortgage bonds:	
Celgar Limited:	
U.S. $52,000,000 6⅛% First Mortgage bonds due January 2, 1981, with an annual sinking fund requirement of U.S. $4,000,000 from 1969 through 1980, less amount included in current liabilities	$49,393,748
Skeena Kraft Limited:	
U.S. $40,000,000 5⅜% First Mortgage and Collateral Trust bonds due July 1, 1985, with annual sinking fund requirements of U.S. $2,000,000 from 1971 through 1975; U.S. $2,500,000 from 1976 through 1980; and U.S. $3,500,000 from 1981 through 1984	43,137,500
	$92,531,248

The first mortgage bonds of Celgar Limited and Skeena Kraft Limited are secured by a fixed and floating charge on the assets of those companies, the net book value of which at December 31, 1968 amounted to $133,567,595 and $76,963,309, respectively.

The trust deeds securing the bonds of Celgar Limited and Skeena Kraft Limited provide that these companies cannot declare or pay dividends, other than stock dividends, or reduce their capital stock, except to the extent of 80% of their consolidated net profit from January 1, 1961 and January 1, 1969, respectively.

The U.S. $11,250,000 6% notes issued by another subsidiary are repayable in annual instalments of U.S. $2,519,500 from 1971 through 1974 with the balance of U.S. $1,172,000 due in 1975. Under certain conditions repayment of up to U.S. $10,078,000 of these notes may be deferred to 1977 and up to U.S. $1,172,000 to 1980.

6. DEFERRED INCOME TAXES:

Depreciation claimed for income tax purposes in 1968 will be less than that recorded in the accounts. Accordingly, the cumulative balance of deferred income taxes of a subsidiary, Celgar Limited, has been reduced during the year by $273,000. Another subsidiary, Skeena Kraft Limited, has not recognized in its accounts future income tax benefits of approximately $11,200,000 which are available for claim against taxes of future years.

7. PREFERRED SHARES OF SUBSIDIARY, CELGAR LIMITED:

Shares issued	$12,500,000
Shares subscribed for and allotted but not issued	2,500,000
	15,000,000
Accrued dividends to June 30, 1968	497,551
Total	$15,497,551

During 1968, the terms of these 7% preferred shares were modified to provide that dividends in arrears at June 30, 1968 of $497,551 are not payable until June 30, 1980. The dividends accrued to June 30, 1968 have been charged to consolidated retained earnings. Dividends are non-cumulative for the period July 1, 1968 to December 31, 1970 but cumulative thereafter. The shares are redeemable by the company at any time provided certain restrictions are complied with but in any event are redeemable on June 30, 1980. The holder, subject to certain restrictions, may require the company to redeem varying numbers of shares at par after June 30, 1975. The holder also may exchange them at par for 7% debentures having substantially the same terms.

8. SHARE CAPITAL:

During 1968 the authorized share capital of the company's common shares was increased from 10,000,000 shares of no par value to 17,500,000 shares of no par value. In July 1968, 3,125,000 common shares were issued in exchange for the minority interest in the issued share capital and subordinated debentures of Skeena Kraft Limited. The excess of the net book value of the assets acquired over the value of the common shares issued of $243,750 has been credited to accumulated depreciation.

The $1.20 cumulative redeemable convertible preferred shares of the company are redeemable at the option of the company at any time at $26 per share, plus accrued dividends. At December 31, 1968 dividends in arrears on these preferred shares amounted to $498,000. The holders of such shares are entitled to convert each $1.20 preferred share into two common shares at any time prior to April 1, 1975. At December 31, 1968, 1,660,000 unissued common shares were reserved for the conversion of the preferred shares.

Changes during 1968 in options outstanding under the company's 1963 stock option plan for officers and employees were as follows:

	Number of Shares	Prices Per Share
Options outstanding at December 31, 1967	34,100	$7.25—8.00
Options granted	20,000	3.25
	14,000	5.375
	34,000	
Options cancelled	(31,600)	3.25—7.25
Options outstanding at December 31, 1968	36,500	3.25—8.00

The options expire at different dates to December 31, 1978 and are exercisable after one year from the date granted to the extent of 20% per year on a cumulative basis. Unallocated shares under the plan totalled 62,700 at December 31, 1968.

The authorized share capital of the company also includes 2,500,000 7% cumulative redeemable preferred shares of $2.00 par value per share. These shares have been issued and redeemed.

9. COMMITMENTS:

At December 31, 1968, annual rental obligations, mainly for logging machinery, equipment and office premises under long-term leases, amounted to approximately $1,150,000 for 1969 and 1970, $1,050,000 in 1971, $850,000 in 1972, $700,000 in 1973 and at reducing amounts year by year to 1985.

10. REMUNERATION OF OFFICERS:

Remuneration of directors and senior officers amounted to $299,687 in 1968 as compared to $352,692 in 1967.

11. CHANGE IN ACCOUNTING POLICY:

The company has changed its method of accounting for mill start-up costs. Previously, the policy of the company was to defer these expenses and to amortize them over five years. It has now been decided that these expenses are to be charged to earnings in the years incurred.

Accordingly, the balance of Consolidated Retained Earnings at December 31, 1966 has been restated to reflect a retroactive charge of $2,030,782 which was the amount of mill start-up expenses incurred to December 31, 1966 of $3,384,637 less the portion applicable to the minority interest in the subsidiary of $1,353,855. Also, the Consolidated Statement of Earnings for 1967 has been restated to reflect net sales, cost of goods sold and other expenses during the mill start-up period, a net expense of $8,921,489, the exclusion of amortization previously recorded of the subsidiary of $2,004,938 resulting in an increase of $6,660,317 in the net loss for the year.

COLUMBIA CELLULOSE COMPANY, LIMITED *and its subsidiary companies*

December 31, 1968

BOARD OF DIRECTORS

Kjell Brandstrom	*Executive Vice President, Svenska Cellulosa Aktiebolaget*
Alexander R. Cochran	*Senior Vice President Staff Services, Celanese Corporation*
Rune Hellerqvist	*Executive Vice President, Svenska Cellulosa Aktiebolaget*
Sverker Kastrup	*Executive Vice President, Svenska Cellulosa Aktiebolaget*
Gay V. Land	*Vice President Corporate Development, Celanese Corporation*
Charles C. Locke, Q.C.	*Partner of the Law Firm of Ladner, Downs, Ladner, Locke, Clark & Lenox, Vancouver, B.C.*
William T. Marx	*Executive Vice President, Celanese Corporation*
George W. Scrimshaw	*President and Chief Executive Officer, Columbia Cellulose Company, Limited*
Hon. James Sinclair	*Chairman of the Board, Lafarge Cement of North America Limited*

OFFICERS

William T. Marx	*Chairman of the Board*
George W. Scrimshaw	*President and Chief Executive Officer*
Clement Garside	*Vice President, Logging and Converting*
W. E. D. Gray	*Vice President and Director of Marketing*
Ronald M. Gross	*Vice President, Planning & Administration, and Secretary*
Frederick Pratt	*Vice President, Finance and Treasurer*
G. Richard Matthews	*Assistant Secretary*
Frederick Slocum	*Controller*

DIVISIONS

Dennis W. Brookes	*Mill Manager, Celgar Lumber Division*
Ian A. Cairns	*Vice President, Castlegar Pulp Operations*
K. Fred Gustafsson	*Vice President, Prince Rupert Pulp Operations*
Ronald R. Jordan	*Vice President, Twinriver Timber Limited*
James D. Sigalet	*Woods Manager, Celgar Woods Division*

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